

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

June 28, 2002

IN RE:

PETITION OF UNITED CITIES GAS FOR  
APPROVAL OF VARIOUS FRANCHISE  
AGREEMENTS

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DOCKET NO. 00-00562

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INITIAL ORDER OF HEARING OFFICER ON THE MERITS

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This matter is before the Hearing Officer of the Tennessee Regulatory Authority (the "Authority") for a decision on the merits with regard to the *Petition for Approval of Various Franchise Agreements* (the "*Petition*") filed by United Cities Gas Company ("United Cities" or the "Company").

**TRAVEL OF THE CASE**

In its *Petition*, filed on June 30, 2000, United Cities requests Authority approval, pursuant to Tenn. Code Ann. § 65-4-107, of franchise agreements contained in ordinances and resolutions passed by three (3) municipalities and one (1) county. As stated in United Cities' *Petition*, the pertinent resolution or ordinance and the terms of each franchise agreement are as follows:

- a) City of Kingsport ordinance effective April 5, 2000 for a term of 20 years;
- b) City of Bristol ordinance effective November 8, 1999 for a term of 30 years;
- c) City of Morristown ordinance effective January 4, 2000 for a term of 15 years;
- d) Maury County resolution effective October 18, 1999 for a term of 30 years.<sup>1</sup>

On August 15, 2000, the Consumer Advocate and Protection Division of the Office of

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<sup>1</sup> *Petition*, June 30, 2000, pp. 1-2.

Attorney General (the "Consumer Advocate") filed a *Petition for Information, Or Alternatively to Intervene* (the "*Petition to Intervene*"). The Consumer Advocate challenged certain provisions regarding franchise fees in the Kingsport, Bristol, and Morristown franchise ordinances. The Consumer Advocate also objected to a provision in the Kingsport ordinance which, the Consumer Advocate stated, purports to impose non pro rata billing of United Cities' customers for franchise fees, in violation of Tenn. Code Ann. § 65-4-105.<sup>2</sup> The Consumer Advocate objected to the Bristol and Morristown franchise agreements, on the grounds that they require United Cities to pay franchise fees to the cities based on gross revenues, which, the Consumer Advocate alleges, violates a recent holding of the Tennessee Court of Appeals, *City of Chattanooga v. BellSouth Telecommunications, Inc.*, No. E1999-01573-COA-R3-CV, 2000 WL 122199 (Tenn. App. Jan. 26, 2000).<sup>3</sup>

The Consumer Advocate requested, pursuant to Tenn. Code Ann. § 65-4-118(c)(2)(B), that the Authority obtain information from United Cities regarding the actual cost to Kingsport, Bristol, and Morristown of the use of their rights of way and facilities by United Cities, and further that the Authority suspend a hearing on the Kingsport, Bristol, and Morristown agreements until United Cities provided information sought by the Consumer Advocate in its *Petition to Intervene*. The Consumer Advocate filed a list of eight (8) questions to be answered by United Cities as an attachment to its *Petition to Intervene*.

At the August 29, 2000 Authority Conference, counsel for the Consumer Advocate informed the Directors of the Authority that the Consumer Advocate no longer objected to or

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<sup>2</sup> *Petition to Intervene*, August 15, 2000, p. 3. The Consumer Advocate has not pursued this objection with regard to the Kingsport agreement in subsequent filings in this docket, during the November 27, 2001 Pre-Hearing Conference, or during the March 14, 2002 Hearing.

<sup>3</sup> *Id.*

sought intervention as to the Maury County franchise agreement.<sup>4</sup> Also, at the August 29, 2000 Authority Conference, the Directors voted unanimously to convene a contested case in this matter and appoint the Authority's General Counsel or his designee as Pre-Hearing Officer, and to grant the Consumer Advocate's *Petition to Intervene* and allow the Consumer Advocate to intervene in this matter as to the Kingsport, Bristol, and Morristown agreements. An Order reflecting this action was issued on October 23, 2000. On October 17, 2000, the Authority received United Cities' response to the questions attached to the Consumer Advocate's *Petition to Intervene*.

On October 26, 2001, United Cities filed a *Motion for Partial Summary Judgment* (the "*Motion*"), and on October 29, 2001, United Cities filed the *Affidavit of Bob Elam* in support of its *Motion*. On November 14, 2001, the Consumer Advocate filed the *Attorney General's Response to United Cities Gas Company's Motion for Partial Summary Judgment* and *Attorney General's Motion for Extension of Time to Respond*. This filing contained a brief discussion of United Cities' *Motion* and requested additional time to file a further response. This request was granted.<sup>5</sup> On November 21, 2001, the Consumer Advocate filed its *Response to Motion for Partial Summary Judgment* (the "*Response*").

On November 27, 2001, a Pre-Hearing Conference was held for the purpose of hearing oral argument on United Cities' *Motion*. Also on November 27, 2001, the City of Morristown ("Morristown") filed a *Motion to Intervene* and a *Memorandum in Support of the City of Morristown's Motion to Intervene*. On November 30, 2001, the Consumer Advocate filed the

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<sup>4</sup> Transcript of Authority Conference, August 29, 2000, pp. 61-62.

<sup>5</sup> *Order Granting Attorney General's Motion for Extension of Time to Respond* (November 16, 2001).

*Attorney General's Response to the City of Morristown's Motion to Intervene.* In its filing, the Consumer Advocate did not object to Morristown's request for intervention, but rather disputed certain comments made in Morristown's *Memorandum* regarding the franchise fees. On December 11, 2001, the City of Bristol ("Bristol") filed the *Motion of City of Bristol to Intervene*. Both Morristown and Bristol have been granted intervention in this proceeding.<sup>6</sup>

On February 15, 2002, the Hearing Officer issued an *Order Denying Motion for Partial Summary Judgment Without Prejudice*, which is discussed below. On March 14, 2002, a Hearing on the merits was held in this matter. The following parties were in attendance:

United Cities Gas Company – **Joe A. Conner, Esq.**; Baker, Donelson, Bearman & Caldwell, 1800 Republic Center, 633 Chestnut Street, Chattanooga, Tennessee 37450

The Consumer Advocate and Protection Division of the Office of Attorney General – **Timothy C. Phillips, Esq.**; 425 Fifth Avenue North, Nashville, Tennessee 37243

The City of Bristol, Tennessee – **Jack W. Hyder, Jr., Esq.**; Massengill, Caldwell and Hyder, P.C., 777 Anderson Street, Bristol, Tennessee 37621

The City of Morristown, Tennessee – **Richard C. Jessee, Esq.**; Bacon, Jessee & Perkins, 1135 West Third North Street, Morristown, Tennessee 37814

On March 14, 2002, Bristol submitted the *Proposed Findings of Fact and Conclusions of Law of City of Bristol*. On April 8, 2002, the Consumer Advocate filed the *Post Hearing Brief of the Attorney General*. On April 15, 2002, United Cities filed the *Reply of United Cities Gas to Attorney General's Post-Hearing Brief*. On April 17, 2002, Bristol filed the *Response of City of Bristol to Post Hearing Brief of the Attorney General*. On April 18, 2002, Morristown filed the *Response of Morristown to Post Hearing Brief of the Attorney General*.

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<sup>6</sup> *Order Granting Motion to Intervene Filed by the City of Morristown* (February 4, 2002); *Order Granting Motion to Intervene Filed by the City of Bristol* (February 4, 2002).

On April 18, 2002, the Consumer Advocate filed the *Reply Brief of the Attorney General*. On April 26, 2002, the Consumer Advocate filed the *Reply Brief and Motion to Strike of the Attorney General*.

## **FRANCHISE FEE PROVISIONS**

### **Kingsport**

The Kingsport agreement is contained in Kingsport Ordinance No. 4742, which was passed by the Kingsport Board of Mayor and Aldermen on March 21, 2000. The term of the Kingsport agreement is twenty (20) years. Section XVIII of Kingsport Ordinance No. 4742 reserves to the City the right to impose a uniform franchise fee applicable to all of the Company's customers, provided all privately owned suppliers of natural gas within the corporate limits of the City are required to pay an identical franchise fee. Such a fee "shall be based upon a percentage of the Company's gross revenues derived from the retail sale of natural gas within the corporate limits of the City."<sup>7</sup> The amount of the fee "shall not exceed the highest franchise fee percentage then in effect under any other franchise of the Company in the State of Tennessee."<sup>8</sup>

### **Maury County**

The Maury County agreement is contained in Resolution No. 21, adopted by the Board of Commissioners of Maury County on October 18, 1999. The term of the Maury County agreement is thirty (30) years. It does not contain a fee provision.

### **Morristown**

The Morristown agreement is contained in Ordinance No. 3022, which was passed by

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<sup>7</sup> Kingsport Ordinance No. 4742, p. 12, attached to United Cities' *Petition*.

<sup>8</sup> *Id.*

the City Council of Morristown on January 4, 2000. The term of the Morristown agreement is fifteen (15) years. Section IX of Morristown Ordinance No. 3022 requires United Cities to “collect and pay annually to the City a sum equal to five percent (5%) of the gross receipts from retail gas sales.”<sup>9</sup>

### **Bristol**

The Bristol agreement is contained in Ordinance No. 99-13, which was passed by the City Council of Bristol on August 5, 1999. The term of the Bristol agreement is thirty (30) years. Section III of Bristol Ordinance No. 99-13 requires United Cities to “pay the City during the remaining term of this franchise an amount equal to six (6%) percent of its annual gross revenues from the sale of the Company’s manufactured, natural or co-mingled gas sold within the City through the system.”<sup>10</sup> Section III further provides that the City “may increase the fee after adoption of this ordinance every then years by an amount of up to one (1%) percent. The fee shall not exceed eight (8%) percent during the term of this franchise.”<sup>11</sup>

### **REQUIREMENT OF AND STANDARDS FOR AUTHORITY APPROVAL**

Tenn. Code Ann. § 65-4-107 provides that no grant of a privilege or franchise from the State or a political subdivision of the State to a public utility shall be valid until approved by the Authority. Approval pursuant to Tenn. Code Ann. § 65-4-107 requires a determination by the Authority, after hearing, that “such privilege or franchise is necessary and proper for the public convenience and properly conserves the public interest.”<sup>12</sup> Tenn. Code Ann. § 65-4-

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<sup>9</sup> Morristown Ordinance No. 3022, p. 4, attached to United Cities’ *Petition*.

<sup>10</sup> Bristol Ordinance No. 99-13, p. 2, attached to United Cities’ *Petition*.

<sup>11</sup> *Id.*

<sup>12</sup> Tenn. Code Ann. § 65-4-107.

107 further provides that in considering such privilege or franchise, the Authority “shall have the power, if it so approves, to impose conditions as to construction, equipment, maintenance, service or operation as the public convenience and interest may reasonably require . . .”<sup>13</sup> Further, in considering a petition for approval of a franchise, as in all other matters, the Authority is prohibited from taking action which is contrary to law. See Tenn. Code Ann. § 4-5-322(h).

### **THE HEARING OFFICER’S RULING ON UNITED CITIES’ MOTION FOR SUMMARY JUDGMENT**

In an order issued on February 15, 2002, the Hearing Officer denied United Cities’ *Motion for Partial Summary Judgment*. The essential part of the holding in that Order, as it pertains to the evidence presented at the March 14, 2002 Hearing, is as follows:

If United Cities produces evidence sufficient to show that the Bristol, Morristown, and Kingsport franchise fee provisions are the result of negotiations between those municipalities and United Cities and United Cities consents to such provisions, United Cities will have established that the provisions were made pursuant to the municipalities’ proprietary capacity. In that event, neither the Court’s decision in *City of Chattanooga* nor any other provision of state law renders a franchise fee based upon a percentage of the utility’s gross revenues per se invalid. If United Cities does not make the requisite showing of negotiations and consent, and it appears that one or more of the franchises alters or revokes pre-existing franchise rights held by United Cities, the municipality must be held to have acted in its governmental capacity, and any franchise fee, to be valid, must be related to the costs incurred by the municipality as a result of the franchise.

Regardless of whether the municipality is determined to have acted in its proprietary or governmental capacity, and regardless of whether the franchise fee is held to be invalid under the Court’s reasoning in *City of Chattanooga*, United Cities must also produce evidence sufficient to show that such franchise fee is in the public interest, in accordance with Tenn. Code Ann. § 65-4-107.<sup>14</sup>

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<sup>13</sup> *Id.*

<sup>14</sup> *Order Denying Motion for Partial Summary Judgment Without Prejudice* (February 15, 2002), pp. 26-28.

The Hearing Officer denied United Cities' *Motion* on the following basis:

On the current state of the record, United Cities' *Motion* for summary judgment as to the Consumer Advocate's objection to the franchise fees on the basis of *City of Chattanooga* cannot be granted. The record does not contain evidence sufficient to show that, as United Cities states, the municipalities were acting in their proprietary capacities. As explained above, such a showing would require evidence that the franchise terms were negotiated between the municipalities and United Cities and not simply imposed upon United Cities, in such a manner as to render the agreements part of the proprietary function under Tennessee law.

Therefore, the Hearing Officer denies United Cities' *Motion* without prejudice. United Cities may proceed to present evidence regarding the franchise agreements, including evidence on the issue of the proprietary capacity, through pre-filed and live testimony. This matter may proceed to a hearing on the merits of United Cities' *Petition*. United Cities may refile its motion for summary judgment at any time. Further, the Hearing Officer finds that unless it can be shown that the municipalities were acting in their governmental and not their proprietary capacities, the Court of Appeals' ruling in *City of Chattanooga* does not render any franchise fee imposed in the franchise agreements invalid as an improper tax.<sup>15</sup>

## **TESTIMONY REGARDING THE FRANCHISE AGREEMENTS**

### **Pre-filed Testimony<sup>16</sup>**

#### **Pre-Filed Testimony of Stephen Brown**

On February 13, 2002, the Consumer Advocate filed the Direct Testimony of Stephen Brown, Ph.D. Dr. Brown's testimony concerning the proposed franchise fees is as follows:

Because no party in this docket has filed any information demonstrating that the fee recovers any costs related to maintaining, improving or administering public rights-of-way, the fee is not cost-based. Therefore, there is no economic justification for United Cities passing the expense to consumers. Those expenses should be excluded from the consumers' bills.<sup>17</sup>

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<sup>15</sup> *Id.*, p. 28.

<sup>16</sup> No pre-filed testimony was submitted regarding the Kingsport or Maury County agreements.

<sup>17</sup> Direct Testimony of Stephen Brown, February 13, 2002, pp. 2-3.



**Pre-filed Testimony of Anthony R. Massey**

On March 11, 2002, Bristol filed the Direct Testimony of Anthony R. Massey, the city manager of Bristol. Mr. Massey described in detail the process that produced the Bristol agreement:

In early 1997, United Cities approached Bristol with a proposed amendment to the 1995 franchise agreement. By letter of January 7, 1997, United Cities notified Bristol of its plan to merge into Atmos Energy Corporation and asked the city to authorize "the transfer of the franchise for a natural gas transmission and distribution system in the City of Bristol, TN, and held by United Cities Gas Company, to Atmos Energy Corporation."

...  
United Cities took the position that its proposed merger with Atmos fell outside the scope of Section XIV of the franchise agreement, and sent the city a legal memorandum in support of this position. The city council directed me to pursue Bristol's option to acquire the gas company's assets. Any purchase by Bristol of United Cities' assets within the city was complicated by the fact that United Cities had a unified system serving both Bristol and its sister city, Bristol, Virginia.

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We then commenced negotiations with United Cities in a effort to reach a settlement by which the city would waive any rights it might have to acquire assets from the gas company under Section XIV of the 1995 franchise agreement and would authorize a transfer of that franchise to Atmos. As part of our negotiations with United Cities, Bristol suggested an amendment to its 1995 lease with the gas company so as to include an additional parcel of real property on which was situated an office building which United Cities intended to vacate.

...  
The proposal of United Cities was generally acceptable to Bristol. Negotiations as to the language for the amended lease continued between attorneys for Atmos and the city.

...  
Finally, in 1999, all issues between Bristol and United Cities were resolved, and language for the amended lease was drafted which was acceptable to both parties. As part of the compromise, Bristol agreed it would use the additional leased tract only as a parking lot and it would not utilize the building for any purpose. At its regular meeting on June 1, 1999, the Bristol city council considered the negotiated amendments to the franchise agreement (Ordinance 99-13) and the lease agreement (Ordinance 99-14) with United Cities.

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The Bristol city council passed both of the ordinances by unanimous (5-to-0) vote at its meeting on June 1, 1999. At its regular meeting on August 5 1999, the Bristol city council held a public hearing on Ordinance 99-13 (amended franchise). No one spoke at the public hearing. A public hearing was also held by the city council on Ordinance 99-14 (amended lease). No one spoke at the public hearing. Each ordinance was passed on final reading by unanimous vote of the city council.<sup>18</sup>

Mr. Massey stated that Bristol did not force the amended franchise agreement on United Cities.<sup>19</sup> Mr. Massey stated, "It was United Cities, not Bristol, that sought in 1997 to amend the 1995 franchise agreement – the gas company first raised the matter of amending the 1995 franchise agreement."<sup>20</sup> Mr. Massey further stated that "[m]ost of the language we used in the amended franchise agreement was proposed by United Cities."<sup>21</sup>

Mr. Massey summarized the franchise agreement as follows:

The obligations under the amended franchise were voluntarily assumed by United Cities, and were not the result of the exercise of a governmental power, but of a contract which both parties could make, and the annual payments agreed to by United Cities were compensation to be paid to the public for United Cities' exercise of the franchise, subject to assent of the city as proprietor of the public streets.<sup>22</sup>

Finally, Mr. Massey lists several objectives that were achieved by the renewed franchise agreement. Among those objectives are the following related specifically to the interests of United Cities:

It settles all issues between the city and the gas company with respect to the Atmos acquisition of United Cities' assets in Bristol.

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It gives the gas company a long-term commitment from the city, assuring the gas company it will have the right to operate in Bristol for the next 30 years and to use the public rights-of-way for its lines during the period.

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<sup>18</sup> Direct Testimony of Anthony R. Massey, March 11, 2002, pp. 4-7.

<sup>19</sup> *Id.*, p. 7.

<sup>20</sup> *Id.*

<sup>21</sup> *Id.*

<sup>22</sup> *Id.*, p. 8.

...

It gives the gas company a strong incentive to invest in additional infrastructure in the city for the long term so as to provide better and expanded gas service to the public.<sup>23</sup>

### **Pre-Filed Testimony of John Collins**

On March 12, 2002, United Cities filed the Direct Testimony of John Collins on Behalf of United Cities Gas. Mr. Collins is the operations manager for the Maryville, Morristown, and Greenville subregion of United Cities.<sup>24</sup> Mr. Collins stated that United Cities' operation benefits United Cities' customers in Morristown, who "rely on United Cities as their principal source of energy to heat their homes, water and to power related natural gas appliances."<sup>25</sup> Mr. Collins testified that in 1999 United Cities approached Morristown with regard to negotiating a new franchise agreement.<sup>26</sup> The agreement current at that time was entered into in 1979 and had a twenty (20) year term and no franchise fee.<sup>27</sup> In 1983, the franchise was amended to impose a five percent (5%) fee.<sup>28</sup> Both the franchise and the amendment were approved by the Tennessee Public Service Commission (the "TPSC").<sup>29</sup>

Mr. Collins stated: "In the normal course of our business, we approached the City of Morristown in 1999 to begin negotiating a new franchise agreement."<sup>30</sup> According to Mr. Collins, Morristown expressed an interest in acquiring United Cities' system, but United Cities discouraged this option.<sup>31</sup> On October 5, 1999, the Morristown city council passed a resolution authorizing negotiations with United Cities with the objective of Morristown's

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<sup>23</sup> *Id.*, pp. 8-9.

<sup>24</sup> Direct Testimony of John Collins on Behalf of United Cities Gas, March 12, 2002, p. 1.

<sup>25</sup> *Id.*, p. 2.

<sup>26</sup> *Id.*

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*, pp. 2-3.

<sup>29</sup> *Id.*, p. 3.

<sup>30</sup> *Id.*

<sup>31</sup> *Id.*

acquiring United Cities' system.<sup>32</sup> United Cities made a presentation at a public hearing on October 26, 1999, in which United Cities explained the "significant advantages in private versus public ownership."<sup>33</sup> On November 16, 1999, the Morristown city council passed a second resolution suspending discussions regarding acquisition of United Cities' system.<sup>34</sup> Representatives of United Cities and Morristown negotiated a new agreement in a meeting held on November 22, 1999.<sup>35</sup> Mr. Collins stated:

We held a lengthy negotiation session and agreed to attempt to incorporate many of the City's concerns in the new franchise agreement. Although United Cities incorporated some of the requests made by the City in the initial negotiation session, some of the requests were simply not acceptable.<sup>36</sup>

Mr. Collins testified that the franchise fee of five percent (5%) was not changed from the 1983 amendment and was not an issue in the negotiations.<sup>37</sup>

#### **Pre-Filed Testimony of Jim Pugh**

On March 12, 2002, United Cities filed the Direct Testimony of Jim Pugh Filed on Behalf of United Cities Gas Company. Mr. Pugh, who is operations supervisor for United Cities, testified with regard to the Bristol agreement. Mr. Pugh described United Cities' operations in Bristol and stated that these operations are in the public interest.<sup>38</sup> Mr. Pugh explained the initiation of negotiations at a point early in the term of the existing Bristol franchise as follows:

In January of 1997 United Cities notified Bristol of its plan to merge into Atmos Energy Corporation and asked the City to authorize the transfer of

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<sup>32</sup> *Id.*

<sup>33</sup> *Id.*

<sup>34</sup> *Id.*, p. 4.

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> Direct Testimony of Jim Pugh Filed on Behalf of United Cities Gas Company, March 12, 2002, p. 1.

the franchise held by United Cities to Atmos Energy. In response the City indicated it would like to discuss the possibility of exercising its first right of refusal to purchase the assets of United Cities in Bristol. In response, United Cities took the position that the proposed merger with Atmos Energy Corporation was not within the scope of the right of first refusal provision in the franchise agreement. United Cities also explained to Bristol that it owned a unified system serving both Bristol, Tennessee and Bristol, Virginia, making separation of the two systems impractical even if the City could acquire the assets under the right of first refusal.<sup>39</sup>

Mr. Pugh described the resulting negotiations, which extended over a two and one-half year period, as follows:

Bristol was interested in amending a 1995 property lease with United Cities in order to include an additional parcel of real property where the office building of United Cities was located. United Cities intended to vacate that building. United Cities proposed to accept the amendment to the lease in conjunction with an amendment to the franchise agreement. The proposed changes to the franchise agreement included: recognition that United Cities was a division of Atmos Energy Corporation; an extension of the 30-year term so as to commence from the date of approval of the new franchise agreement and acceptance by United Cities; an increase in the franchise fee to 6% with provisions limiting the City's ability to increase the franchise fee; a provision specifying that statutory merger, consolidation, recapitalization, or sale or transfer of the common stock of United Cities would not constitute a sale or transfer under Section XIV of the franchise agreement.

The proposal of United Cities was generally acceptable to Bristol subject to the attorneys for the respective parties agreeing on the language. After various drafts, all issues between Bristol and United Cities in regard to the franchise agreement and the amended lease were deemed acceptable.<sup>40</sup>

### **Testimony at the March 14, 2002 Hearing**

#### **Testimony Regarding the Kingsport Agreement**

At the March 14, 2002 Hearing, counsel for United Cities stipulated that approval of the Kingsport franchise agreement would not have precedential effect in the event that

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<sup>39</sup> *Id.*, p. 2.

<sup>40</sup> *Id.*, p. 3.

Kingsport chooses to impose a franchise fee at some future time. Counsel stated that such a fee, if imposed, would require Authority approval.<sup>41</sup>

Mr. Jim Pugh, operations supervisor for United Cities, testified regarding the Kingsport franchise. Mr. Pugh stated that in 2001, United Cities had 4,848 residential customers and 1,066 commercial customers in Kingsport, with annual volume of 1,180,157 mcf.<sup>42</sup> Mr. Pugh stated that United Cities' Kingsport system has 967,523 linear feet of pipe, 725,108 linear feet of which is inside the city limits, and that the majority of this system lies within the public rights-of-way.<sup>43</sup> Mr. Pugh testified that United Cities could not adequately operate, maintain, or replace its distribution system without access to the public rights-of-way, nor could United Cities respond to safety problems, such as leaks, without the access to rights-of-way granted in the franchise agreement.<sup>44</sup>

Mr. Pugh testified that United Cities has a customer support center available at all times to support Kingsport, as well as construction and maintenance employees who work on mains and service lines in the City.<sup>45</sup> According to Mr. Pugh, United Cities has operated for a number of years in Kingsport under numerous franchise agreements.<sup>46</sup>

Mr. Pugh testified that he was personally involved in the process of negotiating the franchise fee at issue in this matter with the City of Kingsport.<sup>47</sup> Mr. Pugh approached the mayor and city manager of Kingsport to discuss a renewal of the franchise, and negotiations ensued between the Kingsport city attorney and representatives of United Cities.<sup>48</sup> The parties

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<sup>41</sup> Transcript of Proceedings, March 14, 2002, p. 8.

<sup>42</sup> *Id.*, p. 11.

<sup>43</sup> *Id.*, pp. 11-12.

<sup>44</sup> *Id.*, p. 12.

<sup>45</sup> *Id.*, p. 13.

<sup>46</sup> *Id.*

<sup>47</sup> *Id.*, p. 14.

<sup>48</sup> *Id.*

to the agreement met twice to discuss revision and outstanding issues, which included repairs to pavement cuts and maintenance work.<sup>49</sup> The agreement was then presented to the Kingsport mayor and board of aldermen, who passed it, and it was accepted by United Cities.<sup>50</sup> Mr. Pugh further stated that, in his opinion, the franchise agreement is necessary and proper to serve the public convenience and properly conserves the public interest.<sup>51</sup> The term of the agreement is twenty (20) years.<sup>52</sup>

Mr. Mike Billingsley, city attorney for Kingsport, also testified at the March 14, 2002 Hearing with regard to the Kingsport agreement. Mr. Billingsley stated that he was the principal negotiator of the agreement on behalf of Kingsport.<sup>53</sup> Mr. Billingsley stated that in 1997, Mr. Pugh reminded him that the existing franchise was ending and needed to be renewed.<sup>54</sup> Mr. Billingsley reviewed various other franchise agreements and concluded that the existing agreement between Kingsport and United Cities was inadequate, particularly with respect to street cuts, a problem created by many utilities and not solely by United Cities.<sup>55</sup> Mr. Billingsley stated that the City determined that it should revise its street cut ordinance and make sure that the United Cities franchise agreement incorporated the revised street cut ordinance.<sup>56</sup> The City considered imposing a franchise fee immediately but determined that it should only reserve the option to impose a fee at a later date.<sup>57</sup> Mr. Billingsley stated that, in his opinion, the franchise agreement is necessary and proper to serve the public convenience

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<sup>49</sup> *Id.*, pp. 14-15.

<sup>50</sup> *Id.*, pp. 15-16.

<sup>51</sup> *Id.*, p. 16.

<sup>52</sup> *Id.*, p. 18.

<sup>53</sup> *Id.*, p. 20.

<sup>54</sup> *Id.*

<sup>55</sup> *Id.*, p. 21.

<sup>56</sup> *Id.*, pp. 21-22.

<sup>57</sup> *Id.*, p. 23.

and properly conserves the public interest in Kingsport.<sup>58</sup> Mr. Billingsley also stated that the agreement was reached through arm's-length negotiation and the City did not threaten to take over United Cities' Kingsport system.<sup>59</sup> Mr. Billingsley stated that he did not believe that the possibility of a franchise fee affected the economic decisions of residential customers.<sup>60</sup>

### **Testimony Regarding the Maury County Agreement**

Ms. Denise Manning, public affairs manager for United Cities, testified with regard to the Maury County franchise. Ms. Manning stated that she was the person authorized by United Cities to assist in obtaining the new franchise agreement from Maury County.<sup>61</sup> Ms. Manning stated that in 2001, United Cities had 12,284 residential customers, 1,342 commercial customers, and 29 industrial customers in Maury County, a total volume of 2,044,473 Mcf, and a total of 1,476,197 linear feet of pipe in its Maury County system.<sup>62</sup> Ms. Manning stated that United Cities has an operating office in Maury County, located in Columbia, Tennessee; this office has full-time employees, including maintenance and service crews, and a twenty-four (24) hour customer support center.<sup>63</sup> Ms. Manning stated that customers in Maury County benefit from United Cities' continuing to supply natural gas through its Maury County distribution system, and United Cities can continue to provide adequate service to Maury County customers in the future.<sup>64</sup> Ms. Manning stated that United Cities would not be able to provide adequate service in Maury County without access to the streets there.<sup>65</sup>

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<sup>58</sup> *Id.*, p. 24.

<sup>59</sup> *Id.*, pp. 25-26.

<sup>60</sup> *Id.*, p. 28.

<sup>61</sup> *Id.*, p. 31.

<sup>62</sup> *Id.*, p. 32.

<sup>63</sup> *Id.*, p. 33.

<sup>64</sup> *Id.*

<sup>65</sup> *Id.*, p. 34.



According to Ms. Manning, the negotiation process for the Maury County agreement consisted of a meeting between Ms. Manning and the county executive for Maury County.<sup>66</sup> She stated that there was no objection to the terms of the agreement, which extends United Cities' franchise for thirty (30) years.<sup>67</sup> Ms. Manning stated that United Cities has operated in Maury County for over thirty (30) years.<sup>68</sup> Ms. Manning further stated that, in her opinion, the franchise agreement is necessary and proper in order to serve the public convenience and properly conserves the public interest in Maury County.<sup>69</sup>

#### **Testimony Regarding the Morristown Agreement**

John Collins, United Cities' operations manager for the subregion of Maryville, Morristown, and Greeneville, testified on behalf of United Cities regarding the Morristown agreement. Mr. Collins stated that he had participated in the negotiation of the Morristown agreement along with other representatives of United Cities.<sup>70</sup> According to Mr. Collins, United Cities has served the Morristown area for over sixty-eight (68) years.<sup>71</sup> Mr. Collins stated that United Cities lines run back and forth between the City of Morristown and surrounding areas in Hamblen County.<sup>72</sup> All of United Cities' Morristown system lies within the public rights-of-way. Mr. Collins stated that United Cities could not operate in Morristown if it did not have the City's permission to occupy those rights-of-way.<sup>73</sup> Mr.

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<sup>66</sup> *Id.*

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*, p. 35.

<sup>70</sup> *Id.*, p. 43.

<sup>71</sup> *Id.*

<sup>72</sup> *Id.*

<sup>73</sup> *Id.*, p. 44.

Collins further stated that, in his opinion, the franchise agreement is necessary and proper in order to serve the public convenience and properly serves the public interest of Morristown.<sup>74</sup>

With regard to the negotiation process, Mr. Collins testified that representatives of United Cities began meeting with Morristown officials in early 1999 to negotiate a new franchise agreement.<sup>75</sup> The existing agreement, enacted in 1979 with a twenty (20) year term, was about to expire.<sup>76</sup> The City was considering several options in 1999, including purchasing the United Cities system and building its own system.<sup>77</sup> United Cities informed the City that it would not sell the system.<sup>78</sup> The City held a public hearing to discuss issues relating to the gas system on October 26, 1999, at which United Cities made a presentation and citizens were allowed to ask questions.<sup>79</sup> The City passed a resolution suspending its investigation into acquisition of the gas system or construction of a separate system by the City; the City did not subsequently raise the issue of buying its own system or condemning the United Cities.<sup>80</sup> Extensive negotiations took place before the parties came to an agreement regarding the franchise.<sup>81</sup> Mr. Collins stated that the franchise fee of five percent (5%) is the same as that imposed when the franchise was amended in 1983.<sup>82</sup> Mr. Collins testified that the City did not advise him at any time that customers in Morristown were objecting to the level of the franchise fee, nor were there any questions or comments from Morristown citizens in regard to the franchise fee.<sup>83</sup>

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<sup>74</sup> *Id.*

<sup>75</sup> *Id.*

<sup>76</sup> *Id.*, p. 45.

<sup>77</sup> *Id.*

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*, p. 46.

<sup>80</sup> *Id.*, pp. 46, 72.

<sup>81</sup> *Id.*, p. 47.

<sup>82</sup> *Id.*

<sup>83</sup> *Id.*, pp. 47-48.

Mr. Collins testified that to his knowledge the highest franchise fee being charged as part of a municipal franchise is five percent (5%), while some municipalities charge no fee.<sup>84</sup> Mr. Collins stated that the term of the Morristown agreement is fifteen (15) years, with an option to renew for two (2) additional five (5) year terms.<sup>85</sup> Mr. Collins stated that United Cities is the only natural gas distribution company in Morristown, although United Cities faces substantial competition from other sources of heating.<sup>86</sup>

The Hon. John Johnson, Mayor of Morristown, also testified regarding the Morristown franchise agreement. Mayor Johnson testified that in 1999, the existing United Cities franchise was expiring, and at the same time United Cities was being acquired by Atmos Energy.<sup>87</sup> Mayor Johnson testified that he and the Morristown city council had received complaints regarding United Cities from Morristown customers.<sup>88</sup> The complaints, which related to "service and method of delivery of service," but not to the franchise fee, arose during the acquisition of United Cities by Atmos Energy, at which time United Cities discontinued its consumer appliance business and closed its Morristown office.<sup>89</sup> In view of the customer complaints, the City considered whether to renew the United Cities franchise or provide gas service through its own gas company.<sup>90</sup> Upon being informed by United Cities that the Company would not sell the system, the city council directed the Morristown utility system to look into the possibility of the City's supplying gas.<sup>91</sup> Following public comment, advertising campaigns, and a public hearing the city council decided to seek a negotiated

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<sup>84</sup> *Id.*, pp. 59-60.

<sup>85</sup> *Id.*, p. 68.

<sup>86</sup> *Id.*, pp. 68, 73.

<sup>87</sup> *Id.*, p. 78.

<sup>88</sup> *Id.*, p. 79.

<sup>89</sup> *Id.*, pp. 79, 105-106.

<sup>90</sup> *Id.*, p. 81.

<sup>91</sup> *Id.*, pp. 81-82.

agreement with United Cities, possibly to include a renewal of the franchise.<sup>92</sup> Negotiations took place, beginning in 1999. In October 1999, the City passed a formal resolution to withhold temporarily its efforts toward acquisition of the United Cities system.<sup>93</sup> Ultimately, Mayor Johnson stated, the negotiations resulted in a new franchise agreement, which was passed by the city council.<sup>94</sup> Mayor Johnson testified that he did not recall any negotiations about the franchise fee.<sup>95</sup> Mayor Johnson stated that “the 5 percent fee was a factor to be weighed, but we did not negotiate it up or down or even consider negotiating it up or down. We took it as a given.”<sup>96</sup>

Mayor Johnson testified that Morristown uses all of the money it receives from the franchise fee for industrial park development, although the franchise fees do not cover all of those expenses.<sup>97</sup> According to Mayor Johnson, Morristown has three (3) major industrial parks, which are a “major feature of how we operate and how we finance and how we supply jobs to our citizens and how we keep their property taxes low by attracting industrial jobs.”<sup>98</sup> Mayor Johnson stated that the City purchases land and makes public improvements, including roads, streets, and sewer and water facilities, for the industrial parks.<sup>99</sup> Mayor Johnson stated that the “county gets about \$2 for every \$1 we do on that [investment in the industrial parks], so the entire region benefits from that industrial expansion funded in portion by this franchise fee.”<sup>100</sup> Mayor Johnson testified that, in his opinion, it is in the public interest and public

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<sup>92</sup> *Id.*

<sup>93</sup> *Id.*, p. 83.

<sup>94</sup> *Id.*, pp. 84, 89.

<sup>95</sup> *Id.*, p. 84.

<sup>96</sup> *Id.*, p. 85.

<sup>97</sup> *Id.*, pp. 85, 93

<sup>98</sup> *Id.*, p. 85.

<sup>99</sup> *Id.*, pp. 86, 91.

<sup>100</sup> *Id.*, pp. 86-87.

necessity for the United Cities franchise to continue.<sup>101</sup> Mayor Johnson admitted on cross-examination that Morristown does not charge a franchise fee to any other provider of energy, only to the cable television company.<sup>102</sup> Mayor Johnson testified that the City did not perform any studies of the costs associated with maintenance of the City's rights-of-way.<sup>103</sup> When asked why it is in the public interest for the City to raise money through franchise fees rather than through property taxes, Mayor Johnson stated that the bulk of the franchise fee in Morristown is paid by industry and business, as the largest consumers of natural gas, and the fee provides money to continue expansion with jobs and industrial activity which benefit consumers.<sup>104</sup> According to Mayor Johnson, customer complaints with regard to United Cities' service "have basically gone away" following the negotiation and passage of the franchise agreement.<sup>105</sup>

#### **Testimony Regarding the Bristol Agreement**

Mr. Jim Pugh testified on behalf of United Cities with regard to the Bristol franchise agreement. Mr. Pugh stated that United Cities has approximately 890,000 linear feet of main serving the Bristol area, of which 409,000 linear feet are outside of the city limits.<sup>106</sup> Mr. Pugh stated that United Cities and its predecessors have operated a gas system in Bristol "quite a number of years."<sup>107</sup> Mr. Pugh testified that in Bristol, United Cities has the same customer service and maintenance capabilities as in Kingsport.<sup>108</sup> According to Mr. Pugh, the majority of United Cities' distribution lines in Bristol lie within the public rights of way, and

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<sup>101</sup> *Id.*, p. 87.

<sup>102</sup> *Id.*, pp. 88-89.

<sup>103</sup> *Id.*, p. 96.

<sup>104</sup> *Id.*, p. 99.

<sup>105</sup> *Id.*, p. 107.

<sup>106</sup> *Id.*, p. 114.

<sup>107</sup> *Id.*

<sup>108</sup> *Id.*

without access to those rights-of-way United Cities would not be able properly to provide service to its customers in the Bristol area.<sup>109</sup>

Mr. Pugh testified that following the announcement of United Cities' proposed merger with Atmos Energy Corporation in January 1997, United Cities approached the City concerning a transfer of United Cities' franchise to Atmos. Mr. Pugh met with Mr. Tony Massey, city manager for Bristol, and discussions were held regarding the City's interest in acquiring United Cities' operations in Bristol.<sup>110</sup> According to Mr. Pugh, the existing franchise agreement gave the City the right of first refusal on purchase of the gas system.<sup>111</sup> On the grounds that the merger with Atmos was not a purchase of the gas system but rather a pooling of assets, United Cities disputed the City's position that the first refusal provisions had been triggered.<sup>112</sup> United Cities explained its position to the City as well as the complexities of the system itself, which stemmed from the fact that it is interconnected with Sullivan County, Tennessee, Washington County, Virginia, and the City of Bristol, Virginia.<sup>113</sup> Mr. Pugh testified that the City was interested in United Cities' local office, which is located adjacent to the city offices and courthouse.<sup>114</sup> According to Mr. Pugh, United Cities was leasing part of its property to the City for a parking area, and the City expressed an interest in acquiring United Cities' building in order to have additional parking.<sup>115</sup> Mr. Pugh testified that negotiations between United Cities and the City resulted in 1999 in an extension

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<sup>109</sup> *Id.*, pp. 114-115.

<sup>110</sup> *Id.*, p. 115.

<sup>111</sup> *Id.*, p. 116.

<sup>112</sup> *Id.*

<sup>113</sup> *Id.*

<sup>114</sup> *Id.*, p. 117.

<sup>115</sup> *Id.*

of United Cities' franchise for an additional thirty (30) years, together with a lease for the parking area the City wanted.<sup>116</sup>

Mr. Pugh stated that the new franchise agreement increased the franchise fee from five percent (5%) to six percent (6%) and capped any future increases at eight percent (8%).<sup>117</sup> Mr. Pugh testified that there are no other companies in Bristol that could provide effective gas service if United Cities could not.<sup>118</sup> Mr. Pugh further testified that United Cities voluntarily agreed to enter into the new franchise agreement.<sup>119</sup> Mr. Pugh testified that the six percent (6%) fee contained in the Bristol agreement is the highest franchise fee he is aware of.<sup>120</sup> Mr. Pugh stated that while United Cities could not "limit" the fee, "in the negotiation process, we attempt to keep it as low as we can because we're competing with alternate fuels."<sup>121</sup> Mr. Pugh stated that the thirty (30) year term of the Bristol agreement is "at the high end of that scale," and the Company prefers longer-term franchises because such franchises provide greater security to investors.<sup>122</sup> When asked why a new agreement had been negotiated after only a few years of the term of the existing agreement, entered into in 1995, had elapsed, Mr. Pugh cited the merger with Atmos and the Company's having opened discussion with the City to get the company name changed in the franchise agreement.<sup>123</sup>

Mr. Tony Massey, City Manager for Bristol, also testified regarding the Bristol agreement. Mr. Massey testified that a franchise agreement between United Cities and Bristol

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<sup>116</sup> *Id.*

<sup>117</sup> *Id.*, p. 118.

<sup>118</sup> *Id.*, p. 119.

<sup>119</sup> *Id.*, p. 120.

<sup>120</sup> *Id.*, p. 131.

<sup>121</sup> *Id.*, p. 129.

<sup>122</sup> *Id.*, p. 132.

<sup>123</sup> *Id.*, p. 133.

was entered into in 1983 with a twenty-five (25) year term.<sup>124</sup> The franchise agreement was renegotiated in 1995, and the 1995 agreement was tied to a lease agreement whereby United Cities leased a parking area to the City, which the public uses to have access to the City municipal building and the Sullivan County Justice Center.<sup>125</sup>

Mr. Massey testified that renegotiation of the franchise began in 1997 following the acquisition of United Cities by Atmos and United Cities' request for a name change.<sup>126</sup> The City's review of the 1995 agreement led the City to conclude that the right of first refusal contained in that agreement had been triggered.<sup>127</sup> According to Mr. Massey, the City "went through an exploratory stage" in which it considered its options, at the same time that the City continued discussions with United Cities.<sup>128</sup> Mr. Massey stated that the City "very quickly realized the complexities in this in that the system was integrated between the two Bristols."<sup>129</sup> The City realized that taking over the system would be difficult because it would "be very difficult to be able to disengage from the Bristol, Virginia, operations and quite costly . . ."<sup>130</sup> Mr. Massey stated:

[A]fter reviewing all of these issues involved with whether or not we wanted to turn it into a public natural gas system, we ultimately decided that it was probably in our best interest not to do that, and so that's why we began the negotiations with the gas company, and this happened to coincide with the gas company vacating the building adjacent to the parking lot where we already had the lease arrangement and also the city's need and the county's need for additional public parking.<sup>131</sup>

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<sup>124</sup> *Id.*, p. 141.

<sup>125</sup> *Id.*, pp. 141-142, 144-145.

<sup>126</sup> *Id.*, p. 145.

<sup>127</sup> *Id.*

<sup>128</sup> *Id.*, p. 146.

<sup>129</sup> *Id.*

<sup>130</sup> *Id.*, pp. 146-147.

<sup>131</sup> *Id.*, pp. 148-149.



Mr. Massey further stated that “through discussions and negotiations with the gas company, it was mutually agreed as a compromise that we would adjust the franchise fee from the 5 percent to the 6 percent” and to reduce the existing cap on the franchise fee from nine percent (9%) to eight percent (8%).<sup>132</sup> With regard to the increase in the franchise fee, Mr. Massey stated that the City “felt that that 1 percent increase was a fair increase to offset our costs for maintaining those public rights of way that United Cities Gas uses.”<sup>133</sup> Mr. Massey stated that the negotiations regarding the new agreement lasted from early 1997 until 1999 and concluded with the adoption of the ordinance approving the new franchise agreement and adoption of a new lease agreement.<sup>134</sup> The adoption process involved two readings of the ordinance and passage following public meetings, which were advertised in the newspaper.<sup>135</sup> According to Mr. Massey, “there was no one from the public objecting to the ordinances.”<sup>136</sup>

Mr. Massey stated that the City’s objective in the negotiations was to “find the best arrangement which was fair to the Bristol citizenry and also fair to the gas company.”<sup>137</sup> Mr. Massey stated that the new franchise agreement benefits the public because it satisfies the City’s need for additional public parking, allows the City “to put to rest the indecision that was out there about this new franchise proposal from the gas company,” and is a “reasonable way to offset our cost for maintaining the public right of ways where there is considerable cost involved.”<sup>138</sup>

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<sup>132</sup> *Id.*, pp. 149-150.

<sup>133</sup> *Id.*, p. 150.

<sup>134</sup> *Id.*

<sup>135</sup> *Id.*, p. 151.

<sup>136</sup> *Id.*

<sup>137</sup> *Id.*

<sup>138</sup> *Id.*, p. 152.

Mr. Massey testified that Bristol charges a franchise fee for cable television.<sup>139</sup> He stated that money the City receives from the United Cities franchise fee goes into the general fund of the City of Bristol to provide services to Bristol's citizens, "including the upkeep and the annual maintenance of our right of ways which has a cost of over \$1 million annually to it."<sup>140</sup> Mr. Massey stated that there is "considerable public investment" in the City's rights-of-way, as well as "considerable annual operating cost" in their upkeep.<sup>141</sup> Mr. Massey stated, "We feel it's certainly proper and appropriate that any private utility that uses that public right of way should help in the maintaining of that public right of way."<sup>142</sup> He stated that the six percent (6%) fee "was an amount that we felt was fair to the gas company and also fair to the citizenry."<sup>143</sup>

Dr. Stephen Brown testified on behalf of the Consumer Advocate. Dr. Brown stated:

My testimony is that the franchise fees are not cost-based. Whether you consider the maintenance of right of ways, the improvements of the right of ways, or even a cost that might be related to the market value of the right of ways. And, therefore, since there is no cost information or basis filed in this case that the franchise fees should not be included in the customers bills; that they should be excluded.<sup>144</sup>

Dr. Brown further stated that there is "no apparent connection between the economic activity that [United Cities is] performing and the franchise fee that they are paying."<sup>145</sup> Dr. Brown stated that his opinion would not be affected by whether a franchise fee was the

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<sup>139</sup> *Id.*, p. 155.

<sup>140</sup> *Id.*, p. 157.

<sup>141</sup> *Id.*, p. 162.

<sup>142</sup> *Id.*

<sup>143</sup> *Id.*, p. 161.

<sup>144</sup> *Id.*, pp. 169-170.

<sup>145</sup> *Id.*, p. 173.

product of an arm's-length negotiated contract between the gas company and the municipality.<sup>146</sup>

## **POST-HEARING BRIEFS**

### **The Consumer Advocate**

In its *Post Hearing Brief*, the Consumer Advocate states:

In the *Order Denying Motion for Partial Summary Judgment Without Prejudice*, date February 15, 2002, the Hearing Officer charged United Cities Gas, and the cities of Bristol and Morristown, with the obligation to prove that the franchise fee was the product of real negotiations and consent. United Cities Gas and the Cities of Bristol and Morristown have failed to do so. Instead, it is obvious from the evidence in this record that the franchise fee was simply imposed upon United Cities Gas by the Cities of Bristol and Morristown.<sup>147</sup>

As grounds for this assertion, the Consumer Advocate states:

The testimony in this matter, indicates that the economic stress that United Cities Gas was working under negates any semblance of real negotiation between the parties of the franchise agreements. United Cities had little choice in this instant [sic] but to capitulate to the demands of the Cities of Bristol and Morristown.<sup>148</sup>

Suggesting that "economic duress" was involved, the Consumer Advocate cites the definition of that term in *Dockery v. Massey*, 958 S.W.2d 346, 348 (Tenn. App. 1997).<sup>149</sup> The Consumer Advocate further states that "United Cities Gas has offered little in the way of proof demonstrating that it had any reason to resist the imposition of franchise fees on its

<sup>146</sup> *Id.*, p. 178.

<sup>147</sup> *Post Hearing Brief of the Attorney General*, April 8, 2002, p. 10.

<sup>148</sup> *Id.*

<sup>149</sup> In *Dockery v. Massey*, the Tennessee Court of Appeals stated that "economic duress . . . has been defined as so coercive and severe that a person of ordinary firmness could not resist it." 958 S.W.2d at 348.

customers.”<sup>150</sup> Noting that United Cities’ “allegiance is to its stockholders,” the Consumer Advocate questions whether the franchise fee causes concern for United Cities.<sup>151</sup>

The Consumer Advocate further states:

The entire circumstances are, of course, complicated by the fact that the city serves two masters: itself (and the general population) and the customers of United Cities Gas who live inside its city limits. The city owes a fiduciary obligation of trust to the customers of United Cities Gas.<sup>152</sup>

The Consumer Advocate goes on to state:

Both the cities and United Cities Gas intimate that they somehow represent the consumers involved. In fact, the cities and United Cities Gas get precisely what each wants at the expense of the customers.

As such, United Cities Gas and the Cities of Bristol and Morristown can not rely on the suggestion that this was an arms-length deal. Therefore, the franchise fee requested must be supported by some type of market analysis reflecting that the rents for the rights of way are reasonable.

In actuality, neither party was concerned about the customers of United Cities Gas. The goals of United Cities Gas and the Cities of Bristol and Morristown move in lock step. Nor were the customers of United Cities Gas represented in the “negotiations.” These parties did not deal at arms-length. *Detroit Auto Dealers Association, Inc. v. FTC*, 955 F.2d 457, 463-464 (6th Cir. 1992).<sup>153</sup>

Under the heading “Remedies,” the Consumer Advocate states:

Although United Cities Gas and the Cities of Bristol and Morristown cite the *City of Chattanooga vs. BellSouth Telecommunications* case as allowing it to charge a franchise fee in excess of the costs for maintaining the rights of way, it is clearly an expansion on Tennessee case law to suggest that the franchise fee need not relate to the rental values of the rights of way. In other words, without some type of reasonable value placed on the rights of way, the franchise fee is essentially arbitrary and inconsistent with current Tennessee law and

<sup>150</sup> Post Hearing Brief of the Attorney General, April 8, 2002, p. 11.

<sup>151</sup> *Id.*

<sup>152</sup> *Id.* The Consumer Advocate cites for this principle *Fleming v. City of Memphis*, 148 S.W. 1057 (Tenn. 1912); *McCay v. Du Pont Rayon Co.*, 96 S.W.2d 177 (Tenn. App. 1935); and *Board of Directors of St. Francis Levee Dist. v. Bodkin*, 69 S.W. 270 (Tenn. 1902).

<sup>153</sup> Post Hearing Brief of the Attorney General, April 8, 2002, pp. 11-12.

reasonable public policy. The correct approach is to require some type of support for the fee. The rates must be reasonable. Tenn. Code Ann. § 65-5-201.

If neither United Cities Gas nor the cities involved are able to substantiate the subject franchise fee as reasonable then the petition should be denied or altered by removing the fee all together [sic].<sup>154</sup>

### United Cities

In its *Reply*, filed on April 15, 2002, United Cities states:

The testimony at the hearing in this matter clearly established that Morristown and Bristol obtained United Cities' consent to the franchise fees through negotiations before the fees were included in the franchise agreements. As such, it cannot be argued that the cities were acting in anything but their proprietary capacities, and the fees are valid. The testimony also established that the franchise agreements are necessary for the public convenience and properly conserve the public interest.<sup>155</sup>

United Cities states that the Consumer Advocate "focuses on whether the testimony established that the cities were acting in their proprietary capacity."<sup>156</sup> United Cities states:

The governing law in this case was concisely set forth in the Authority's February 15 Order: if the franchise fees were included in the agreements as a result of negotiations and were consented to by United Cities, the fees did not impair or revoke previously existing franchise rights and were thus within the cities' proprietary capacity. In its brief, the Attorney General concedes that the franchise agreements were negotiated, but argues that the fees were not the result of "arms-length" negotiations because they were colored by the "economic stress" that United Cities was under. Even assuming the Attorney General's characterization of the negotiations were correct (which the testimony directly contradicts) it makes no difference. The standard is whether there were negotiations and consent, not whether the negotiations were "arms length" or free from economic realities. The testimony clearly established that, unlike the franchise fee in the BellSouth case, which was imposed by ordinance and not accepted by the utilities, the Bristol and Morristown franchise fees were part of a franchise agreement freely negotiated and consented to by both parties.<sup>157</sup>

<sup>154</sup> *Id.*, pp. 12-13.

<sup>155</sup> *Reply of United Cities Gas Company to Attorney General's Post-Hearing Brief*, April 15, 2002, p. 6.

<sup>156</sup> *Id.*, p. 3.

<sup>157</sup> *Id.*

Further, United Cities responds to the Consumer Advocate's argument that "the Authority should . . . consider the 'reasonableness' of the fee and that the fee must have some relation to the rental value of the rights of way."<sup>158</sup> Noting that the "sole authority the Attorney General cites in support of this proposition is the statutory rate-making provision, Tenn. Code Ann. § 65-5-201," United Cities states:

That statute has no relevance whatsoever to the determination of the validity of franchise fees imposed by municipalities. The statute gives the Authority the power to fix just and reasonable rates to be **imposed by public utilities**. Tenn. Code Ann. § 65-5-201. It does not restrict in any manner the franchise fees **imposed by municipalities**, nor does it impair the municipalities' statutory right to impose franchise fees set forth in Tenn. Code Ann. §§ 65-26-101 and 65-4-105(e) and repeatedly affirmed by the Tennessee Supreme Court in Nashville Gas & Heating Co. v. City of Nashville, 152 S.W.2d 229 (Tenn. 1941) and Lewis v. Nashville Gas & Heating Co., 40 S.W.2d 409 (Tenn. 1931).<sup>159</sup>

United Cities further states:

There is no authority whatsoever for the Attorney General's assertion that the franchise fees must be reasonable or somehow related to the rental value of the streets. In fact, the Tennessee Supreme Court has specifically held numerous times that the franchise fees "may be a definite sum arbitrarily selected." City of Nashville, 152 S.W.2d at 233; Lewis, 40 S.W.2d at 413.<sup>160</sup>

United Cities states that the Consumer Advocate's objections to the franchise agreements for Bristol and Morristown "boil down to a pure policy argument," that argument being "that it is unfair that the cities and utilities together set the amount of the franchise fee that is ultimately paid by the consumer."<sup>161</sup> United Cities states that "[h]owever 'unfair' the Attorney General may think it is, that is the legal framework that has been structured by the

<sup>158</sup> *Id.*, p. 4.

<sup>159</sup> *Id.*, pp. 4-5. (Emphasis in original).

<sup>160</sup> *Id.*, p. 5.

<sup>161</sup> *Id.*

legislature and the Tennessee Supreme Court.”<sup>162</sup> United Cities cites Tenn. Code Ann. §§ 65-26-101 and 65-4-105(e), as well as *City of Chattanooga*, 2000 WL 122199 at \*1; *Nashville Gas*, 152 S.W.2d at 233; and *Lewis*, 40 S.W.2d at 413.

### **Bristol**

In the *Proposed Findings of Fact and Conclusions of Law of City of Bristol*, filed on April 16, 2002, Bristol lists a number of legal principles, with citations, in support of the proposed franchise agreements. Bristol focuses particularly on the franchise agreements as an aspect of the City’s municipal powers. Bristol cites a number of cases for the principle that a City is the proprietor of its streets and rights-of-way and administers those streets and rights-of-way in its proprietary capacity.<sup>163</sup> Bristol further states:

Whether to allow a private enterprise to use public property, and the compensation to be paid by such enterprise to the public, are matters “of judgment to be exercised by the duly elected City officials,” and their decision will be upheld in the absence of a showing that such “is contrary to the public interest, that it represents a misuse or abuse of the discretion and authority of the Board of Commissioners, or that it is in any other way Ultra vires or beyond the legitimate charter powers of the City.” State ex rel. Association for Preservation of Tennessee Antiquities v. City of Jackson, 573 S.W.2d 750,755 (Tenn. 1978).<sup>164</sup>

In addition, Bristol cites Tenn. Code Ann. § 65-4-106(e) and *Lewis* in support of the City’s power to charge a franchise fee.<sup>165</sup>

<sup>162</sup> *Id.*

<sup>163</sup> *Proposed Findings of Fact and Conclusions of Law of City of Bristol*, April 16, 2002, p. 12. Bristol cites *Fleming v. City of Memphis*, 148 S.W. 1057 (Tenn. 1912); *McCay v. DuPont Rayon Co.*, 96 S.W.2d 177 (Tenn. App. 1935); *Humes v. Mayor & Aldermen of Knoxville*, 20 Tenn. 304 (Tenn. 1839); and *Board of Directors of St. Francis Levee Dist. v. Bodkin*, 69 S.W. 270 (Tenn. 1902).

<sup>164</sup> *Id.*

<sup>165</sup> *Id.*, pp. 14-16.

### **The Consumer Advocate's Motion to Strike**

In its *Reply Brief and Motion to Strike*, filed on April 26, 2002, the Consumer Advocate moved to strike the Response filed on April 18, 2002 by Morristown on the grounds that it was not timely filed. The Consumer Advocate also took the opportunity in its April 26, 2002 filing to restate at length its arguments concerning the proposed franchise agreements. Morristown's *Response* is largely a summary of the evidence presented at the March 14, 2002 Hearing. It is dated April 17, 2002, and was received by the Authority on April 18, 2002. The Hearing Officer does not believe that either party's rights are unduly prejudiced by simply disregarding the statements made in both filings.

### **FINDINGS AND CONCLUSIONS**

As stated in the February 15, 2002 *Order*, in order to establish that the requirement of the proposed franchise fees in the Bristol and Morristown agreements is made under the proprietary function of those cities, United Cities must demonstrate that the fees resulted from negotiation and were not unilaterally imposed upon United Cities.<sup>166</sup> Otherwise, United Cities would have to show a connection between each fee and the costs to each city resulting from United Cities' use of that city's rights-of-way.<sup>167</sup> If such a connection could not be made, the fees would be barred as improper taxes under *City of Chattanooga*.<sup>168</sup>

The Hearing Officer finds that United Cities and the Cities of Bristol and Morristown have presented sufficient evidence to demonstrate that the fees and the agreements as a whole are the result of fully bilateral, "arm's length" negotiations. Neither the proposed fees nor any

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<sup>166</sup> *Order Denying Motion for Partial Summary Judgment Without Prejudice* (February 15, 2002), pp. 26-28.  
<sup>167</sup> *Id.*  
<sup>168</sup> *Id.*



other provisions were unilaterally imposed upon United Cities. One must not mistake rigorous bargaining for coercion.<sup>169</sup>

Because the franchise fee provisions are made under the cities' proprietary functions, it is not necessary to determine whether the fees are based on the cities' costs. Aside from the specific issue of whether the proposed fees run afoul of *City of Chattanooga*, however, there is the question of whether the agreements are in the public interest. The Hearing Officer finds that United Cities has presented sufficient evidence to demonstrate that all four (4) of the proposed franchise agreements are in the public interest. This finding includes the proposed franchise fees for Bristol and Morristown.

All four (4) of the proposed franchise agreements continue longstanding franchise arrangements in communities where United Cities has extensive operations that rely on use of the public rights-of-way. These franchise arrangements have been and continue to be of mutual benefit to United Cities, its customers, and the communities. All four (4) of the agreements are for extensive terms that will lend stability to the relations between United Cities and the communities. The Maury County agreement is undisputed and is in the public interest for that county. The Kingsport agreement is also undisputed and is in the public interest. The franchise fee provided for in the Kingsport agreement will not be imposed without prior Authority approval. The Morristown and Bristol agreements resolve issues arising from the acquisition of United Cities by Atmos. The franchise fees contained in the Bristol and Morristown agreements are used for worthy municipal purposes. The Bristol and Morristown agreements are in the public interest. There has been no public objection to the proposed franchise fees. Further, the determination by the relevant City that the franchise fee

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<sup>169</sup> The negotiations certainly do not reflect "economic duress," as defined in *Dockery v. Massey*.

is in the public interest must be accorded substantial weight, within the bounds discussed below. Accordingly, the four (4) franchise agreements are approved pursuant to Tenn. Code Ann. § 65-4-107.

The Hearing Officer is not persuaded by the Consumer Advocate's arguments on either the governmental/proprietary distinction or the public interest issue. The Consumer Advocate has not seriously disputed the existence of or the witnesses' descriptions of the negotiations. The Consumer Advocate has instead rehashed arguments that were dismissed in the February 15, 2002 Order. The Consumer Advocate has not shown that the proposed agreements are contrary to the public interest and has barely attempted to make such a showing except on grounds that have been rejected.

In making this decision, the Hearing Officer is not holding that any franchise fee, no matter how high, is in the public interest. A point may be reached where the requirement of a franchise fee is not in the public interest, even though the utility and the municipality may agree that it is proper. The reason is obvious: at some point, the franchise fee will simply render the utility's rates burdensome to the consumer. At such a point, notwithstanding the principle that the municipality is generally a good determiner of the public interest for its citizens, an excessive fee would violate the public interest requirement of Tenn. Code Ann. § 65-4-107. It is of some concern that the Bristol franchise fee has increased. The newly imposed cap of eight percent (8%) offers some assurance that United Cities will not accept indefinite increases in franchise fees, but at the same time this cap suggests that further increases may take place.

The Hearing Officer is of the opinion that the six percent (6%) fee contained in the Bristol agreement is not patently unreasonable. Ample evidence exists in the record to

demonstrate that this fee is in the public interest and is employed for purposes that benefit the public interest in Bristol. However, there is, at present, no evidence to demonstrate that an increase beyond six percent (6%) pursuant to Paragraph III of the Bristol agreement is similarly in the public interest. Pursuant to the authority granted in Tenn. Code Ann. § 65-4-107, the Hearing Officer determines that any increase in the Bristol franchise fee beyond the six percent (6%) fee approved herein shall not be valid until approved by the Authority.

Finally, the conclusion that the franchise fees at issue in this case meet the standards for approval set forth in Tenn. Code Ann. § 65-4-107 is primarily a legal conclusion which does not exhaust all potential policy concerns that the franchise fees may raise. Of greatest concern in this case the six percent (6%) fee approved for Bristol. This is, according to the record in this case, the highest paid by United Cities. It is also higher than any fee previously approved for United Cities by the Authority or the TPSC. Viewed from a primarily legal perspective, this fee does not appear to be unreasonable or improper, but a more policy oriented analysis may lead to a different conclusion. The Authority's Directors are better situated to make such policy judgments, and the Hearing Officer recognizes that the Directors may deem it appropriate to make such judgments themselves with regard to any proposed franchise fees, particularly any fees proposed in the future that exceed five percent (5%).

**IT IS THEREFORE ORDERED THAT:**

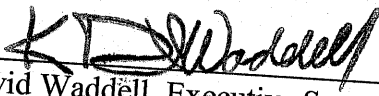
1. The proposed franchise agreements between United Cities Gas Company and the Cities of Bristol, Kingsport, and Morristown, and Maury County are approved.
2. Any increase in the Bristol franchise fee beyond the six percent (6%) fee approved herein shall not be valid until approved by the Authority

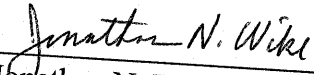
3. Any party aggrieved by the Hearing Officer's decision in this matter may file a Petition for Reconsideration with the Hearing Officer within fifteen (15) days from the date of this Order.

4. Any party aggrieved by the decision of the Hearing Officer in this matter may file a Petition for Appeal with the Tennessee Regulatory Authority within fifteen (15) days from the date of this Order.

5. In the event this Order is not appealed to the Directors of the Tennessee Regulatory Authority within fifteen (15) days, this Order shall become final and shall be effective from the date of entry. Thereafter, any party aggrieved by the decision of the Hearing Officer, may file a Petition for Review in the Tennessee Court of Appeals, Middle Section, within sixty (60) days from the date of this Order.

ATTEST:

  
K. David Waddell, Executive Secretary

  
Jonathan N. Wike, Hearing Officer